

Betting On Biotech

Rendering courtesy of JLL

The BioMed Realty Trust Inc.'s i3 campus is a \$146 million, 316,000-square-foot speculative building project. The project will finish in July of this year and be occupied in July 2017.

Life Sciences' Need for Space Spurs Developers to Pursue Spec Projects

BY KATIE CALLAHAN

The high demand for biotech office space in San Diego is boosting the confidence of traditionally cautious landlords. Rather than waiting to build a project until a tenant is lined up, life science construction companies are building sprawling campuses



Robert Betz

based on speculation alone.

That confidence is warranted, it seems, as tenants are often lining up before the project finishes, said **Robert Betz**, executive vice president of operations for **McCarthy Building Cos.**

"There's not a single job we finished that ended up empty or where we had the landlord going out and looking for a tenant," Betz said. "That's not happening in the market I'm seeing. There's always someone involved or in mind."

According to **JLL**, the first quarter of 2016 and the fourth quarter of 2015 saw 10 speculative construction projects each, compared with none in 2010. Speculative construction projects are those completed without a lease signed yet.

Betz's company is finishing up the **BioMed Realty Trust Inc. (BMR)** speculative, \$146 million i3 campus, a 316,000-square-foot development. The lease agreement for this space was signed

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Financial Planning for Life Science Executives

Corporate executives within the life science industry face many unique wealth management challenges and opportunities. Along with running a successful company and answering to shareholders and a board of directors, they also have complex earnings packages, concentrated stock positions and a high likelihood of liquidity events — which can be financially complex. Managing this complexity is increasingly difficult within today's environment due to SEC regulations and the constantly evolving and complex nature of business' lifecycles.

Though these challenges exist, the potential for high dollar value transactions is high. We saw positive growth and returns over the last few years, yet the last 12 months showed decreased activity and returns in the sector for San Diego. This creates an opportunistic time to gift stock to children and grandchildren so the future appreciation is out of the estate. A grantor can give stock outright or, through another common technique called a Grantor Retained Annuity Trust (GRAT). A GRAT is a useful planning tool if a security is expected to increase in value substantially during the term of the GRAT, thereby getting all taxable appreciation out of the grantor's estate. The grantor of the GRAT receives a yearly annuity in the amount of the initial gift plus interest, and any appreciation of the stock over the interest rate goes to the beneficiary free of gift tax.

It is imperative to put a financial plan in place and have it continually monitored to allow for changing life events, new opportunities and market dynamics. Executives in life science companies may consider a 10b5-1 trading plan. A 10b5-1 trading plan allows an executive to set up pre-determined times to sell stock over a specific price beyond a specific date in the future. These plans must be set up during open windows but



trade executions can occur during blackout periods. Given that many life science executives have fewer trading windows than other industries due to more information flowing within senior management that is nonpublic, pending mergers and other milestones, a 10b5-1 plan is sometimes critical.

Charitable gifting of shares may be considered particularly when the stock is not undervalued. Gifting appreciated securities provides an additional benefit from avoiding capital gains tax.

The peace of mind offered by a well-constructed financial plan is invaluable to help clients navigate periods of uncertainty during liquidity events. Although a concentrated equity position in the current San Diego life science environment can be daunting, the financial planning process offers an executive and their family clarity, direction and discipline.

Callan Capital does not provide individual tax or legal advice. Clients should review planned financial transactions and wealth transfer strategies with their own tax and legal advisors. For more information, please refer to our most recent Form ADV Part 2A which may be found at www.adviserinfo.sec.gov.



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at the start of the second quarter and named genomics giant **Illumina Inc.** its tenant. Construction is slated for completion in July.

Most of the tenants Betz is seeing are trying to consolidate or make their organizations more efficient by moving or redeveloping existing spaces for a campus environment or feel, whereas before they might just lease whatever space they could find. This is leading to more repeat clients.

In addition, brokers said landlords are more willing to gamble by starting construction early because the current market shows a surplus of tenants looking for office and lab space. The market easily absorbs that demand with speculative building and redevelopment.

Meeting Demand

Grant Schoneman, vice president at JLL and a part of the life sciences group, an international group of brokers that specializes in the sector, said that while speculative building has always been around, the change occurred about 12-15 months ago.

“It (speculative construction) has not been as prevalent as it is in today’s marketplace,” he said. “You have this waning supply and in order to get supply up and be able to deliver space for when tenants need to occupy it, you need to start construction before the lease is in place.”

According to JLL, there was a huge surge in speculative construction from

the fourth quarter of 2015 to the first quarter of 2016, with 760,500 square feet of speculative construction completed. Approximately 50 percent of the total construction activity in the first quarter of 2016 was speculative and approximately 50 percent was built for a tenant, with construction completed after a tenant signs a lease for a building.

In the first quarter of 2015, 316,262 square feet was speculative construction, which was the i3 campus, and 63,000 of that was built for a tenant. That’s a stark contrast from this quarter where 1,456,370 square feet was speculative or built for a tenant.

The most popular biotech buildings in the market right now range in size from 40,000 to 100,000 square feet and there are 1.1 million square feet of redevelopment projects under construction. Last year, there was more activity among a smaller tenant base with 800,000 square feet of former office buildings redeveloped into life science buildings with lab and office spaces.

Lacking Large Spaces

Ted Jacobs, director of **Cushman & Wakefield’s** global life sciences practice group in San Diego, said for tenants needing 50,000 square feet or more, there are not that many opportunities because those spaces have already been leased, so there may only be one to three properties that could work for that tenant. Because of this, rents are on the rise from landlords who understand the difficulty to find space.

“This could be a life science opportu-



Photos provided by JLL

Construction was started before the current lease, with medtech giant Illumina Inc., was in place. This was a large deal for San Diego. Generally, speculative construction, or building a project without a lease in place, is rare.

nity,” he said. “We’ve been talking about running out of space in San Diego for years. There’s new redevelopment every year. But this is the first time in five-plus years where landlords are going spec. It’s very rare, building on space without a tenant in tow. They have to do it that way; if you don’t go spec, you can miss out on opportunities. There is a lot of competition, depending on size range.”

Jacobs said much of the supply being completed now is already under contract.

Speculative building, which they haven’t seen in over a decade, could give tenants more opportunity to relocate in the future.

“We’re seeing a lot of early recasts and renewals just because there’s not a lot of opportunity to relocate. If they’re able to approach landlords in a time period where it’s foreseeable that you could possibly relocate, they’re going to be more aggressive on trying to keep you. Landlords don’t want vacancies even if the market is very tight; they’re motivated to keep the tenant.”



Grant Schoneman



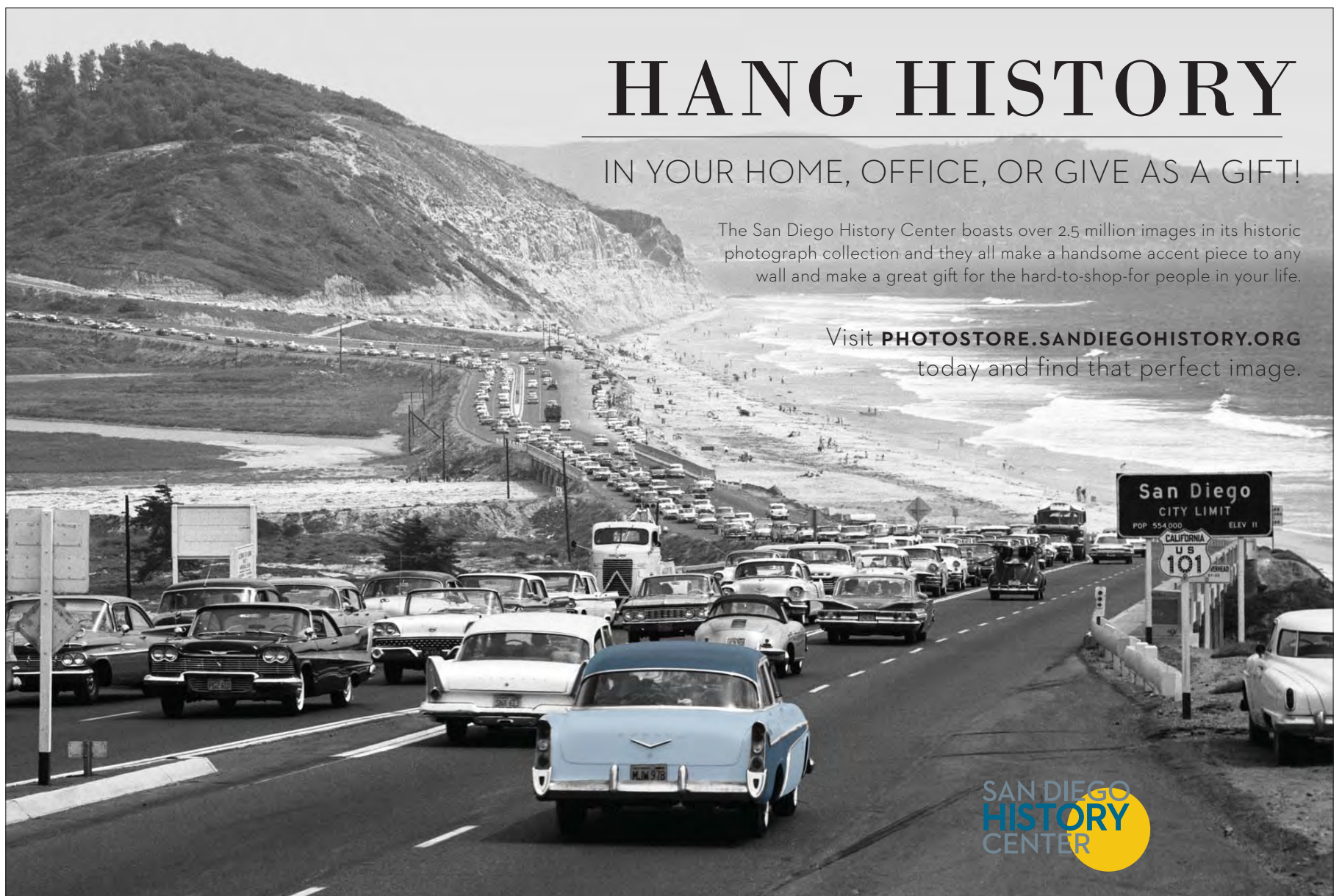
Ted Jacobs

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